No. 9809

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

NELSON TAYLOR, J. R. MASON, GILBERT MOODY, and N. O. BOWMAN,
Appellants,

vs.

PROVIDENT IRRIGATION DISTRICT,
Appellee.

BRIEF FOR APPELLEE.

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PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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PRELIMINARY.

In appellants' opening brief, counsel has admittedly and intentionally gone "outside the record" and in many instances has distorted the facts appearing in the record.

The only objection raised to the plan of composition in the District Court was the point now argued by counsel as appellants' first proposition in which it is contended that the "plan is unfair and discriminatory as to the creditor, appellant Nelson Taylor, in that it does not provide for payment of his three bonds with accrued interest in full". Pursuant to counsel's request a special finding was made on this issue and the District Court found that the plan of composition was

not unjust, unfair or discriminatory in any respect. (R. 203-204.)

Appellants offered no evidence in the District Court other than two annual statements of appellee Provident Irrigation District. (R. 118, 191.)

Thirty-one points on appeal and assignments of error were filed by appellants. (R. 215-219.) Six propositions are argued in appellants' opening brief.

STATEMENT OF THE CASE.

The appellee Provident Irrigation District, hereafter referred to as the District, was organized in May, 1918, comprising 22,805 acres of land situated in the Counties of Glenn and Colusa, State of California, and overlapped by Reclamation District No. 2047.

On August 15, 1918, the District issued its First Issue of bonds in the total principal amount of $1,000,000.00 scheduled to mature serially on the 15th day of August in each of the years 1930 to 1949, and on August 9, 1921, the District issued its Second Issue of bonds in the total principal amount of $190,000.00 scheduled to mature serially on the 1st day of July in each of the years 1922 to 1933, all of said bonds bearing interest at the rate of 6 per centum per annum payable semiannually. (R. 2-3.)

The District was organized and its original bonds were issued during the "rice boom days" of World War I when the price of rice ranged from $4.50 to $8.50 per hundred pounds. The price of rice "crashed"

in 1920 and thereafter dropped to a low of 65¢ per hundred pounds. During the past ten years the price of rice has fluctuated between the low of 65¢ to a high of $1.65 per hundred pounds. (R. 101-102, 106, 110-111.)

The lands of the District are "low-lying heavy clay with some adobe" subject to overflow in the winter. Approximately 9,900 acres, now excluded from the District boundaries, are unfit for anything other than pasture and the remaining lands are adaptable principally to growing rice which can only be profitably raised every other year on the better lands and only every third year on the poorer lands. (R. 14, 74, 99, 100, 102, 109, 127-129.)

Immediately after the "crash" of rice prices in 1920, a large portion of the lands went out of production entirely resulting in financial difficulties to the District. (R. 102, 110.) In 1933 Mr. H. E. Vogel, a member of the California Irrigation Districts Securities Commission since 1931, made an investigation of the District and his report thereon states in part as follows:

> "* * * It is doubtful, if proper appraisals were made of the fertility of the soils of this District before the loan was granted by the bankers for construction of the irrigation system, and again at the time the bond issue was floated. Approximately 75 per cent of the acreage is in the trough of the Colusa Basin, and most of the additional 25 per cent is unsuitable for general crops, and there have been no net returns given to the land except in a few years of especially high rice prices. By the year 1921 the people north of P. B. Cross had

failed to meet their assessment, and some of the large Oakland banks with whom Cross had dealt, were forced to pay up the delinquencies to protect their lands. By 1922, delinquent bond coupons were also taken up by the Central National Bank of Oakland. Since 1924, delinquent assessments have been increasing at a rapid rate until for the year 1932 and 1933 practically all the lands were delinquent. The highest number of holdings in the District was in 1924, when assessments were levied on thirty-seven ownerships, twenty-eight of which were less than four hundred acres. Since that time the number of assessments has decreased until in 1932 there were only ten ownerships, mostly in the hands of banks." (R. 132-133.)

Between the years 1927 and 1938 the District acquired title through delinquent assessment sales to all of the lands within its boundaries except approximately 350 acres. (R. 99, 111-112, 133.) Title to the lands in the District was also acquired by the State of California and Reclamation District No. 2047 through delinquent county taxes and assessments. (R. 99.) In 1936, prior to the undertaking of reorganization of the District, the total obligation against the lands, in addition to the bonded debt of the District, was $652,485.02. (R. 100.)

In January, 1933, the District was in default in the payment of bond principal in the amount of $68,000.00 and in default in the payment of interest coupons in the amount of $169,433.00, disregarding the interest accrued on registered matured bonds and coupons. (R. 133.) At the time of filing the petition in the present

proceeding, the total principal amount of bonds outstanding was in the sum of $957,000.00, of which amount $341,000.00 was matured. Unpaid and matured interest coupons totaled the sum of $415,192.50. (R. 3-4.)

In July, 1936, the District employed Mr. Charles F. Lambert as its fiscal agent in connection with a proposed reorganization and refinancing program and an application for a loan from the Reconstruction Finance Corporation, hereafter referred to as R. F. C., was filed. This application was denied in September, 1936. Thereafter a complete study of the District was made and after the conclusion in 1939 of certain litigation between the District and some of its bondholders, an application was made to the R. F. C. for reconsideration of the District's former loan application. (R. 68-70.) The reorganization and refinancing of the District was complicated by the joint ownership of practically all of the lands within the District by the State of California and Reclamation District No. 2047, and the necessity of clearing all of the liens. (R. 99.)

On the 20th day of December, 1939, the R. F. C. granted a loan to the District in the amount of $193,500.00, the sum of not to exceed $2100.00 to be used for expenses. The loan was made subject to certain special conditions providing that the District reduce its acreage to approximately 13,000 acres, settle and discharge all overlapping liens on the lands remaining in the District and apply all surplus funds on hand at the date of disbursement and all subsequent net funds derived from the sale of District lands to the

reduction of the indebtedness except as might be provided by the Division Chief of the R. F. C. (R. 70-98.) The loan was to provide payment of 20¢ on the dollar of principal amount of the outstanding bonds, exclusive of interest. (R. 72-73.)

The loan was accepted by the District on the 2nd day of January, 1940, and on the same date a plan of composition of its outstanding indebtedness was adopted. (R. 141-143, 11-18.) The plan provided for the payment to the bondholders of 20 cents for each dollar of principal amount of the bonds held by them respectively, provided that all unpaid interest coupons maturing on or after July 1, 1931, were delivered with said bonds. Certain deductions were provided for coupons not attached. (R. 15.) The resolution found that "a portion only of the outstanding coupons maturing on and prior to the 1st day of January, 1931, have been paid in full" (R. 14) and in order to equalize the interest payments to the respective bondholders, it was provided "that for each coupon maturing on or prior to the 1st day of January, 1931, that may be surrendered or deposited in accordance with this plan, the depositor thereof shall receive the full face value thereof". (R. 16.) The payments on account of the principal of the bonds were to be paid from the R. F. C. loan and the payments of interest coupons were to be paid from funds of the District. (R. 16.)

At the time of the hearing in the District Court over 94% of the outstanding bonds had been deposited by the bondholders under the plan. (R. 59-67.) A disbursement had been made by R. F. C. to the depositing

bondholders and the claim of R. F. C. duly filed in the District Court. (R. 49.) The only remaining objectors to the plan are the appellants who represent approximately 3.3% of the outstanding bonds of the District. (Appellants' Opening Brief, pages 10-11.)

The uncontradicted evidence shows, and the District Court found, that the District was insolvent and that "the plan of composition as offered by the petitioner herein is fair, equitable and for the best interests of its creditors, and does not discriminate unfairly in favor of any creditor or class of creditors". (R. 4, 201, 109, 134-135, 175.)

Under the plan of composition, the reorganized District will have an average bonded indebtedness of approximately $14.50 per acre (R. 107-108) and the evidence is uncontradicted that "the land could not carry any additional load, and cannot carry this load if agricultural conditions turn any more adverse than they have in the last five years. This whole plan is all predicated on the last five years' basis, in order to strike an average and to take into consideration the value of crops produced. Costs of production have come down, making it more feasible now; in my opinion, ten years ago it could not have been done, for the reason that the cost of production was so much higher than it is today. Machinery and new methods have come in, making it possible to grow rice at a lesser cost than before". (R. 109, 134-136, 174-175.)

Pursuant to the requirements of the loan grant from the R. F. C., the District excluded from its boundaries 9924.25 acres of land, the non-agricultural land herein-

above referred to. The land remaining within the District boundaries and owned by the District was sold for an average price of approximately $10.00 per acre the proceeds of which were used to clear the land of the obligations of Reclamation District No. 2047 and the State of California on a scaled down basis and to pay the coupons maturing on or prior to January 1, 1931, which obligations totaled approximately $334,512.98. (R. 99-101, 120.) The delinquent county taxes against the property remaining within the District was settled for about 10 cents on the dollar (R. 103) and the title of Reclamation District No. 2047 was purchased by the District at auction sale, some bonds of the Reclamation District being used as a part of the purchase price. (R. 125.)

The excluded lands are owned jointly by the District, Reclamation District No. 2047 and the State of California, the total debt burden against the lands, disregarding the District's indebtedness, being $339,972.00. (R. 105.) The excluded land "has no value considering all of the debts that are on the land, that is the County, and the Reclamation District, and the Irrigation District, and that if the land was sold and prorated according to the interest, the debts each has against it, that the land has practically no value to anyone". (R. 128-129.) The District had on hand at the time of the hearing in the District Court the sum of $22,000.00 which sum had to be used for the operations of the District and no assessments are payable until December, 1941. The superintendent of the District, T. E. Balch, testified: "We have to go pretty

easy to get along with that. We really need more than that." (R. 173-174.) The structures of the District have deteriorated and additional work on them will be required. (R. 107, 172, 173.)

Prior to the undertaking of the refinancing program, the bonds of the District were selling at prices ranging from 5 to 10 cents on the dollar. (R. 113.)

ARGUMENT.

I.

ANSWER TO FIRST PROPOSITION: "THE PLAN IS UNFAIR AND DISCRIMINATORY AS TO THE CREDITOR, APPELLANT NELSON TAYLOR, IN THAT IT DOES NOT PROVIDE FOR PAYMENT OF HIS THREE BONDS WITH ACCRUED INTEREST IN FULL."

The contention of appellant Nelson Taylor is based upon the erroneous premise that by reason of the presentation and endorsement of his bonds after they matured in accordance with the provisions of Section 52 of the California Irrigation District Act, he was "entitled to separate classification as a creditor".

On page 29 of appellants' brief, it is stated:

> "The irrigation district law of California plainly provides as to any district that payment to its bond creditors shall be made in the order of presentation. Bates v. McHenry, 123 C. A. 81; Provident Land Corporation v. Zumwalt, 12 Cal. (2d) 365."

Identically the same contention was made by the non-consenting bondholders, some of whom were repre-

sented by Mr. Cook, in the leading case of *West Coast Life Ins. Co. v. Merced Irrigation District,* 114 Fed. (2d) 654, 672-674, decided by this Court on the 5th day of September, 1940. The *Bates* and *Zumwalt* cases, supra, cited by counsel, and several other cases were distinguished, and after a comprehensive discussion of the subject the point was concluded as follows at page 674:

> "We are convinced that there is no phase of unfairness to a plan of composition under the Bankruptcy Act by reason of including in one class matured and registered and unpaid bond obligations with unmatured bond obligations all of which for payment in regular course depend upon the taxing power of a district. *It places all such creditors whose claims are payable from the same source on a basis of absolute equality.*" (Italics ours.)

In *Moody v. James Irr. Dist.,* 114 Fed. (2d) 685, decided by this Court on the same day as the *Merced* case, supra, in which case also Mr. Cook was counsel for some of the appellants, it is stated at page 688:

> "* * * we decided in the Merced case that due bond interest and principal does not become preferred claims when presented and registered as provided by Section 52 of the California Irrigation District Act. Had the District proceeded in its course as a solvent entity the holders of overdue bonds and interest would have been paid in accordance with Section 61a of the California Irrigation District Act. But it did not and could not have so proceeded, and it resorted to the Bankruptcy law for relief."

There is nothing in the plan of composition that is discriminatory against the appellant Nelson Taylor. (R. 15-16.) The plan is general and applies exactly the same to all bondholders and under the foregoing authorities it is wholly immaterial whether the unpaid bonds are matured or unmatured, registered or unregistered.

On page 29 of appellants' brief, it is stated:

> "* * * The only reason that the three bonds of Nelson Taylor were not paid in the order of presentation and that subsequent bonds and coupons were paid was that the district deliberately and unlawfully withheld payment on the asserted theory (Tr. pp. 181, 189) that the bonds had outlawed, and continued that stand until the decision in the case of *Moody v. Provident Irrigation District* in which it was determined that the presentation of bonds to the treasurer prevents the statute of limitations from running until the treasurer has funds and notifies the bondholders. But even then the district continued its refusal to comply with the law."

This statement, although immaterial, is not entirely correct. The District did in 1935, prior to any attempted reorganization, pay two one thousand dollar bonds ahead of Mr. Taylor's bonds under the mistaken theory that they were outlawed. (R. 118, 181.) The *Moody* case referred to by counsel did not settle the question of the statute of limitations until November, 1938. (*Moody v. Provident Irrigation District,* 12 Cal. (2d) 389, 85 Pac. (2d) 128.) It is not true, however, that if the *two* bonds had not been paid, then Mr.

Taylor's *three* bonds would have been paid. The record shows that after the payment of the *two* bonds there was only $45.00 in the bond fund until the year 1939 when a landowner made a redemption amounting to approximately $5500.00 and no payments have been made from this money. (R. 195.)

The three bonds of Mr. Taylor were all presented for payment on the 30th day of January, 1931, and in the absence of sufficient money to pay them and other bonds presented prior thereto or on that date, the District would have been without authority to pay any of them. Section 52 of the California Irrigation District Act provides as follows:

> "* * * If money is not available in the fund designated for the payment of any such matured bond or interest coupon, it shall draw interest at the rate of seven per cent per annum from the date of its presentation for payment until notice is given that funds are available for its payment, and it shall be stamped *and provision made for its payment as in the case of a warrant for the payment of which funds are not available on its presentation.*" (Italics ours.)

Section 61a of the California Irrigation District Act provides for the payment of warrants where funds are not available to pay them on their presentation as follows:

> "* * * Whenever there is sufficient money in the treasury to pay *all* such outstanding warrants *or* whenever the board of directors shall order that *all* such warrants presented for payment *prior to a certain date,* be made and there is sufficient

> money available for such payments, the treasurer shall give notice * * * stating that he is prepared to pay *all* warrants of the district for the payment of which funds were not available upon their original presentation, *or all* such warrants which were presented for payment *prior to the date fixed by the board of directors, as the case may be.* * * *" (Italics ours.)

It is apparent, therefore, that even though the *two* bonds had not been paid in 1935, the appellant Taylor still would not and could not have been paid on his *three bonds, or any of them.* The fact that the *two* bonds were paid in 1935 does not affect the rights of appellant Taylor any more than it affects the rights of all of the other bondholders of the District. On the contrary, to pay Mr. Taylor in full with accrued interest would give him an unjustified preference and priority over all of the other bondholders, both consenting and nonconsenting.

On page 10 of appellants' brief the statement is made that three interest coupons owned by appellant Taylor and maturing on August 15, 1930, "are not payable under the plan although subsequent coupons of all other bonds due January 1, 1931 are so payable * * *." This is not correct. The plan expressly provides for the payment of all coupons "maturing on or prior to the 1st day of January, 1931". (R. 16.)

At the request of counsel the District Court made a special finding on the issue presented as to appellant Taylor's bonds which finding concludes as follows:

"* * * that it is true that under the plan of composition of petitioner respondent Taylor will be required to accept and take 20 cents on the dollar for his said $3000.00 of bonds, but it is not true that said plan is unjust or unfair or discriminatory for that reason, or for any other reason, or at all."

II.

ANSWER TO SECOND PROPOSITION: "THE EVIDENCE WAS INSUFFICIENT TO SUPPORT THE FINDING OF THE COURT THAT THE PLAN IS FAIR AND EQUITABLE AND FOR THE BEST INTEREST OF THE CREDITORS, AND THE FINDINGS DO NOT SUPPORT THE DECREE AS RESPECTS THIS QUESTION."

We will answer the contentions of appellants in the reverse order stated in the foregoing second proposition:

A. THE FINDINGS AMPLY SUPPORT THE DECREE.

Counsel's contention that the findings do not support the decree is not supported by any argument other than the mere statement of the proposition. The record is clear that the findings amply support the decree.

In reference to the insolvency of the District and the fairness of the plan, the District Court specifically found that "the petitioner is insolvent or unable to meet its debts as they mature" and that "the plan of composition as offered by the petitioner herein is fair, equitable and for the best interests of its creditors, and does not discriminate unfairly in favor of any creditor

or class of creditors". (R. 201.) The District Court further found that all of the allegations contained in the District's petition were true in which the facts involved are set out in more detail. (R. 202, 1-8.)

Obviously the District Court found only the ultimate facts, and suffice it to say that similar findings were approved in the following cases decided by this Court in all of which Mr. Cook was counsel for some of the objecting bondholders:

West Coast Life Ins. Co. v. Merced Irrigation District, supra (114 Fed. (2d) 654, 677);

Bekins v. Lindsay-Strathmore Irr. Dist., 114 Fed. (2d) 680, 685;

Moody v. James Irr. Dist., supra (114 Fed. (2d) 685, 689).

B. THE EVIDENCE IS SUFFICIENT TO SUPPORT THE FINDING OF THE COURT THAT THE PLAN IS FAIR AND EQUITABLE AND FOR THE BEST INTEREST OF THE CREDITORS.

The argument of counsel on this point is predicated upon the fallacious assumption that the same rules are applicable here as are applicable in a private bankruptcy proceeding.

The principal case relied upon by counsel is *Consolidated Rock Products Company v. Dubois,* 61 S. Ct. 675, 85 L. ed. 603, involving the bankruptcy of a private company and two of its wholly owned subsidiaries, the rule of which has no application to the case at bar.

In *Newhouse v. Corcoran Irr. Dist.,* 114 Fed. (2d) 690, decided by this Court on the same day as the *Merced Irrigation District* case, supra, Mr. Cook again

being counsel for some of the appealing bondholders, it is stated at page 690:

> "Throughout appellants' briefs the principle of ordinary or private bankruptcy that the assets of the bankrupt, including his property, must be effectively applied to the debts, is sought to be applied to the situation before us. *The bankruptcy of a public entity, however, is very different from that of a private person or concern.*" (Italics ours.)

The primary question to be determined in considering the fairness of a plan of composition of a public district is: What debt load can the lands of the District reasonably bear? In order to carry out any plan of composition a district "must be in a position to proceed as a going District". (*Moody v. James Irr. Dist.,* supra (114 Fed. (2d) 685, 689).)

We have heretofore set out the financial history of the District and the obstacles confronting the District in attempting to refinance and reorganize on account of the long default and joint ownership of almost all of the lands by the District, Reclamation District No. 2047 and the State of California. We have already seen that the District was placed in financial difficulties as early as 1921 and that by 1933 practically all of the lands were delinquent. (R. 99, 132-133.) Between 1936 and 1939 "a complete study had been made of the Provident District, studies from the standpoint of the land within the boundaries of the District, as to its classification, soil, and productivity, and the economics connected with the irrigation of the land" (R. 69), the

assessment history of the District, the value of crops produced, and "a complete study of bond values". (R. 111, 113.) The plan evolved was based upon averages as to the ability of the lands to pay. (R. 111.)

Mr. Charles F. Lambert, fiscal agent of the District in charge of the refinancing, testified (R. 109):

> "Q. Is that land able to carry a greater load than will be put against it under this new bond issue?
>
> A. I would say not. I would say that the land could not carry any additional load, and cannot carry this load if agricultural conditions turn any more adverse than they have in the last five years. This whole plan is all predicated on the last five years' basis, in order to strike an average and to take into consideration the value of crops produced. Costs of production have come down, making it more feasible now; in my opinion, ten years ago it could not have been done, for the reason that the cost of production was so much higher than it is today. Machinery and new methods have come in, making it possible to grow rice at a lesser cost than before."

Mr. H. E. Vogel testified that he had been associated with irrigation districts for many years and since 1931 had been a member of the California Districts Securities Commission and during that time had made investigations of various irrigation districts. (R. 130-131.) Mr. Vogel first became acquainted with the District in 1933 at which time he made an investigation of the financial affairs of the District and prepared a report based thereon. A portion of this report is

quoted from in our "Statement of the Case" and for the sake of brevity we will not again set it out. (R. 131-133.) In 1936, 1937, 1938 and 1939, Mr. Vogel made an investigation and a report of the District's affairs for the California Districts Securities Commission. (R. 134.) Mr. Vogel further testified:

> "Q. As to the ability of the land to pay, in your opinion could this land pay on any greater valuation than has been placed on it, with this $14.50 bond issue against the land?
>
> A. All we can go on is the past experience and estimate the future. I don't believe that the District could stand, in the way of all its obligations, any greater load. One principal reason is that the District is not adapted for general crops, in other words the range of crops that can be grown within the district is very limited. This land is very shallow, most of it clay soil, and water will not penetrate into the soil. It is unsuited even for grain, because it is either too wet or too dry, most of the time to grow crops, and the grain would either be drowned out or else it doesn't produce it for the lack of moisture." (R. 134-135.)

> "Q. Now would you say that the plan is or is not fair and equitable and for the best interest of the creditors?
>
> A. I believe it is for the best interest of the creditors because it looked very hopeless for a long time for the creditors to get anything out of their bonds. At least, in passing judgment on it, I thought it was fair and equitable. I thought it was about the most they could realize from their investment." (R. 136.)

Mr. T. E. Balch, superintendent of the District since 1928, testified as to the conditions of the structures of the District and as to the cost of additional rehabilitation work (R. 172-173), the cost of raising rice (R. 176), and corroborated the testimony of Mr. Lambert and Mr. Vogel in reference to the ability of the lands to pay assessments. (R. 174-175.)

The only cash on hand in the District is the sum of $22,000.00 all of which will be required for the operation of the District. (R. 173-174.) The only other asset of the District is the excluded lands which are owned jointly by the District, Reclamation District No. 2047 and the State of California, and which have a total debt burden, aside from the District's indebtedness, of $339,972.00. (R. 105.)

All of the foregoing evidence is uncontradicted and undisputed as the appellants did not offer any evidence in the District Court except two annual statements of the District which were only for the purpose of showing that the District paid two bonds in 1935.

In *Jordan v. Palo Verde Irr. Dist.,* 114 Fed. (2d) 691, decided by this Court on the 20th day of September, 1940, the plan of composition of the District provided for the payment to its bondholders of 24.81 cents on the dollar of the principal amount of their bonds. The objecting bondholders, some of whom were represented by Mr. Cook, contended that the District was able to make "a vastly more generous payment to bondholders". In affirming the decree of the District Court approving the plan, this Court stated at page 695:

> "* * * The trial court's conclusion as to the fairness of the plan was supported by two agricultural economists, one connected with the University of California and the other connected with R. F. C., and these economists took into consideration the probable ability of the land to pay for a period of thirty years projected into the future. We think the plan is fair and for the best interests of the creditors."

In *Moody v. James Irr. Dist.,* supra (114 Fed. (2d) 685), the situation presented was quite similar to the case at bar except that in the *Moody* case the District had on hand cash totaling $98,886.56. The indebtedness of the District was slightly in excess of $1,000,000.00 and the plan of composition provided for payment of 24.976 cents on the dollar of principal amount of bonds provided that the bondholders furnished to the District their proportionate amount of Reclamation District No. 1606 bonds, which District overlapped the Irrigation District, in order to pay off the Reclamation District debt. In affirming the judgment of the District Court approving the plan of composition, this Court stated at page 689:

> "It is argued by appellants that the plan is unfair for the reason that the funds on hand show that the amount to be paid upon each item of indebtedness could well be greater than that provided by the plan. The point seems not to have been presented in the trial court, which found that the plan is 'fair, equitable and for the best interests of its creditors * * *'.
>
> "The evidence shows that Mr. H. E. Vogel, long a resident of Fresno County, California, and a

member of the California Districts Securities Commission testified (we quote from the agreed statement): 'That, judging from past history, he thought that the indebtedness of $256,500 provided for in the plan of composition was well up to the limit of the ability of the lands in the District to meet.'

"It must be remembered that this is not a proceeding in liquidation and the principles to be applied must differ somewhat from such a proceeding. In liquidation it is perfectly evident that the creditors would get almost nothing. To afford the plan of payment proposed the District must be in a position to proceed as a going District and for this reason its cash in hand cannot be too greatly depleted."

III.

ANSWER TO THIRD PROPOSITION: "THE PLAN OF COMPOSITION IS UNFAIR."

A. THE PAYMENT OF COUPONS MATURING ON OR PRIOR TO JANUARY 1, 1931, AT FACE VALUE. (COUPON NO. 25 AND EARLIER.)

Counsel does not contend that the principle of equalizing the interest payments up to and including the 1st day of January, 1931, is in any manner unfair, but on page 39 of appellants' brief, the absurd statement is made that:

"* * * This part of the plan is unfair because it appears to the appellants that by pre-arrangement the benefit of this payment goes largely to certain individuals who are connected with the

> Provident Land Corporation and not to the bondholders. It appears from the entire record that the major part of the coupons due January 1, 1931, by some mysterious means found themselves in the hands of George McKaig."

Counsel then states on page 40 of appellants' brief that he does not contend "that there was anything improper or unfair that he (McKaig) should have been the recipient of such benefits". The record does not show how many No. 25 coupons were deposited by Mr. McKaig or what arrangement there may have been between Mr. McKaig and the Provident Land Corporation. The record does show, however, that Mr. McKaig deposited a total of $520,000.00 in bonds and that the Provident Land Corporation did not deposit any. (R. 67.) Mr. McKaig must have had a large number of the No. 25 coupons with these bonds, but there was no "pre-arrangement" as to who would receive the proceeds of any of the bonds or coupons as between the District and anyone. The District did not control or have any voice in the internal affairs of the Provident Land Corporation.

Counsel further states that "full disclosure was not made to all of the parties of this situation and that the bondholders did not realize the real significance of their not having coupon No. 25 attached to their bonds when they turned them in". Full disclosure was made to all of the bondholders of the District in the notice of time and place for hearing petition for confirmation of the plan of composition wherein it was expressly stated that the plan provided "for the pay-

ment at face value of each coupon maturing on or before the 1st day of January, 1931". (R. 53-55.)

None of the bondholders who deposited their bonds are complaining and the record shows that appellant Nelson Taylor has a No. 25 coupon for each of his three bonds (R. 40-41), appellant Gilbert Moody has a No. 25 coupon for each of his three bonds (R. 42-43), appellant J. R. Mason has no No. 25 coupons which means that he has either already been paid or that he has disposed of them in a manner satisfactory to himself (R. 51-52), and the claim of N. O. Bowman is not in the record. The record further shows that 48 No. 25 or earlier coupons are in the hands of persons whose names and addresses are unknown to the District. (R. 26-28.)

B. LANDS EXCLUDED FROM THE DISTRICT.

On page 40 of appellants' brief it is stated that some 10,000 acres of land is to be arbitrarily taken out of the district without adequate reason being shown therefor. As we have heretofore stated, 9924.25 acres of land have already been excluded from the District for the reason that it is unfit for anything other than pasture and the loan grant from R. F. C. expressly required its exclusion. (R. 74, Special Condition No. 1, 129.)

Counsel "suspicion" and state that appellants "believe" the excluded land will be purchased by the Biological Survey at a price from $7.00 to $15.00 per acre netting to the District "from $75,000.00 to $100,000.00" although there is not the slightest support in the record

for any such "suspicion" or "belief". Reference is also made to the "so-called Spaulding Ranch" which is not in the District and never has been and has no bearing whatever upon this case.

The uncontradicted testimony of Mr. Lambert shows that "the land has no value considering all of the debts that are on the land, that is the County, and the Reclamation District, and the Irrigation District, and "that if the land was sold and pro-rated according to the interest, the debts each has against it, that the land has practically no value to anyone". (R. 128.) Mr. Lambert further testified on cross-examination:

> "Q. * * * How much is the land worth with the taxes off, suppose there was no debt burden against it, how much is the land worth as land?
>
> A. $5.00 an acre with no tax obligation.
>
> Q. Has it any value for agriculture?
>
> A. It has no agricultural value, that is why we threw it out of the District. It is pasture land." (R. 129.)

The debt burden of Reclamation District No. 2047 and the delinquent County taxes amount to a total of $339,972.04 against these excluded lands. (R. 100.)

Counsel also intimate that money will be accruing to the District from the sale of "the lands to be left within the District". On page 15 of appellants' brief, note 8, it is stated:

> "Special condition No. 3 (Tr. p. 75), requires the district to turn in all this money to the R. F. C. At $10 an acre the amount would be over $120,000, which when deducted from $193,500 leaves a

> meager sum still outstanding. Besides this there is the prospective sale to the Biological Survey of land intended for exclusion from the district."

Counsel apparently is under a complete misapprehension as to what has happened. The evidence shows that the land remaining within the District has already been sold for $10.00 per acre and the proceeds thereof used to clear up the indebtedness of Reclamation District No. 2047 and the County tax indebtedness on a scaled down basis and to pay the coupons maturing on or prior to January 1, 1931, totaling approximately $339,972.00. Special Condition No. 3 of the R. F. C. loan grant (R. 75) required the discharge of "the lien of overlapping drainage indebtedness" and the settlement of *ad valorem* taxes on the lands remaining in the District. The total cash on hand in all funds of the District at the time of the hearing in the District Court was $22,000.00, all of which was needed for operation expenses. (R. 173-174.) Special Condition No. 3, referred to by counsel required "all surplus funds on hand at the date of disbursement, and all subsequent net income from the sale of land owned by the Borrower" to be used to reduce its indebtedness.

C. INDEBTEDNESS OF RECLAMATION DISTRICT NO. 2047.

On page 42 of appellants' brief, it is stated that the District paid Reclamation District No. 2047 $350.00 per $1000.00 bond, whereas it only offers $200.00 per $1000.00 bond in its plan of composition. This is not correct and the Reclamation District indebtedness is not involved in the plan. The title of the Reclamation

District was purchased "by auction sale at the court house". It was not a settlement with the bondholders of the Reclamation District. (R. 124-125.) A similar contention was made in the *Merced Irrigation District* case, supra (114 Fed. (2d) 654), and the Court held at page 674 that the "obligations * * * of overlapping agencies are simply not affected by the plan". (See also, *Moody v. James Irr. Dist.,* supra (114 Fed. (2d) 685, at pages 688-689).)

D. BUREAU OF RECLAMATION REPORT.

On pages 42 and 43 of appellants' brief, counsel argues that a report of the Bureau of Reclamation shows that "the over-all per acre cost of nine projects authorized, with a total cost of $14,622,000, is $165" and concludes that "the only answer is to deny the fairness of the plan in this case". We fail to get the point.

E. PAYMENTS TO THE FISCAL AGENT.

Counsel's next point is that "the plan is unfair because it allows over $20,000 in fees for the fiscal agent".

Mr. Lambert, the fiscal agent for the District, was employed by the District in July, 1936 (R. 68), and testified that:

> "A. During 1936 they (the District) paid me $2,000.00. Subsequent thereto and to the completion of my work, including the reorganization and refinancing, the sale of all these lands up there, the total amount I received has been $20,300.00, for which I may explain to the Court I have also

> paid my own expenses, there has been no expenses paid by anyone during that four year period." (R. 112-113.)

No objection to the amount paid to Mr. Lambert was made by counsel in the District Court and the payment was approved by the Court. It is apparent that when consideration is given to the fact that the services of Mr. Lambert extended over a period in excess of four years and that he paid his own costs and expenses, the amount paid was conservative.

F. LEASING OF DISTRICT OWNED LANDS.

On page 45 of appellants' brief without any support from the record, it is stated:

> "* * * With any effort at all the land could be operated by the district officials on a lease basis and out of the proceeds the expenses of operation paid, and a return made to the bondholders."

In other words, the appellants desire that the District continue to operate the land, keeping it off the tax rolls and paying no part of Governmental expenses.

This is proven by counsel's citation of the case of *Anderson-Cottonwood v. Klukkert,* 13 Cal. (2d) 191, and he states that because the lands are owned by the District they can be no longer taxed by the County or other public agency and concludes that the "total return, therefore, from the land could be applied, after payment of the operating expense of the district, to liquidation of the indebtedness". This does not follow. Practically all of the lands, before the reorganization

plan, were owned jointly by the District, Reclamation District No. 2047 and the State of California. All of these titles are of equal rank (*La Mesa etc. Irr. Dist. v. Hornbeck,* 216 Cal. 730, 17 Pac. (2d) 143), but the State has priority to possession and to leasing of the lands. Section 3773 of the Political Code provides:

> "Notwithstanding any other provisions of law to the contrary, the State, by and through the Controller, shall have the sole and exclusive power and authority to lease and rent, and to receive and collect all rents, issues and profits arising in any manner from property heretofore or hereafter deeded to the State pursuant to the provisions of section 3785 of this code, which power and authority shall accrue from and after the date of recording of the deed to the State."

It is apparent therefore that the plan suggested by counsel could not be carried out even assuming it was feasible, which it is not.

Counsel again quote from various governmental reports which have no bearing on the case at bar and require no answer.

G. ACCEPTANCE OF PLAN BY 94% PLUS OF THE OUTSTANDING BONDHOLDERS.

On page 49 of appellants' brief it is stated that "the Court based its conclusion in this case very largely upon the fact that 94% of the bonds had accepted the plan. For this reason alone the cause should be reversed". We have already pointed out the evidence upon which the Court based its findings and conclusions and no further answer seems necessary.

IV.

ANSWER TO FOURTH PROPOSITION: "THE COURT ERRED IN FAILING TO FOLLOW THE LOCAL LAW APPLICABLE TO THIS DISTRICT AND WHICH WAS THE LAW OF THE CASE."

A. PAYMENT OF BONDS AND COUPONS IN THE ORDER OF REGISTRATION.

Counsel's first point under his fourth proposition, argued from pages 50 to 55 of appellants' brief, is the same as that advanced in the first proposition, that is, that the bonds of the District should be paid in the order of their presentation and registration by reason of Section 52 of the California Irrigation District Act and reliance is again placed upon the case of *Provident Land Corporation v. Zumwalt,* 12 Cal. (2d) 365, 85 Pac. (2d) 116.

This point is fully answered in our answer to first proposition and we will not burden the Court with a repetition of that argument here.

B. LANDS OF THE DISTRICT AS IMPRESSED WITH A TRUST.

Counsel's second point, argued from pages 55 to 59 of appellants' brief, is that the lands within the District "are impressed with a trust" for the benefit of the bondholders and that "the land can never be released from the obligation to pay the balance due".

This same contention was made in the case of *West Coast Life Ins. Co. v. Merced Irr. Dist.,* supra (114 Fed. (2d) 654), and decided adversely to the objecting bondholders. (See pages 675 and 676.)

Similar contentions are also rejected in:

Bekins v. Lindsay-Strathmore Irr. Dist., supra (114 Fed. (2d) 680, 683, 684);

Jordan v. Palo Verde Irr. Dist., supra (114 Fed. (2d) 691, 694, 696).

V.

ANSWER TO FIFTH PROPOSITION: "THE PLAN ON COMPOSITION IS NOT PRESENTED IN GOOD FAITH."

Counsel doubts the propriety of the argument on this point. He should. The argument is out of place and counsel's conduct in advancing it inexcusable. We will not dignify it by a reply.

VI.

ANSWER TO SIXTH PROPOSITION: "THE PLAN OF COMPOSITION IS NOT SUPPORTED BY LOCAL LAW."

Counsel has, under this point, confused the "plan for the refunding of bonds of the District" adopted by the District on the 20th day of January, 1940, pursuant to the requirements of the R. F. C. loan grant and the "plan of composition" adopted by the District on the 2nd day of January, 1941. The "plan for the refunding of the bonds of the District" has only to do with the issuance of refunding bonds to the R. F. C. in accordance with the loan grant and that plan is approved by Order No. 10 of the Districts Securities Commission referred to by counsel. (R. 149-154.)

The plan of composition provides for the payment of 20 cents for each dollar of principal amount of bonds "provided that all unpaid interest coupons maturing on or after July 1, 1931, are delivered with said bonds", and further expressly recites:

> "* * * and provided, further, that for each coupon maturing on or prior to the 1st day of January, 1931, that may be surrendered or deposited in accordance with this plan, the depositor thereof shall receive the full face value thereof.
>
> "That such payments will be made from the proceeds of a loan which has been authorized by the Reconstruction Finance Corporation and which will be disbursed to or for the benefit of the District for the purpose of reducing and refinancing its indebtedness, as provided in the resolution of said Corporation authorizing said loan, except that all payments made on account of coupons maturing on or prior to the 1st day of January, 1931, shall be made from funds of said District other than proceeds of said loan." (R. 16.)

Order No. 11 of the Districts Securities Commission, not mentioned by counsel, expressly provides:

> "(1) That consent is hereby given to the filing in the District Court of the United States for the Northern District of California of a petition for the confirmation of the plan of composition of outstanding indebtedness of Provident Irrigation District *as adopted by the said Board of Directors on January 2, 1940;* * * *" (R. 20.)

As a matter of fact, there is no requirement in the law that the Districts Securities Commission approve a plan of composition under the Bankruptcy Act.

CONCLUSION.

In conclusion we submit that the decree of the District Court approving the plan of composition of the District Court should be affirmed.

Dated, Willows, California,
August 6, 1941.

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